

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

In the Matter of:

AN INQUIRY INTO INTRALATA TOLL)	
COMPETITION, AN APPROPRIATE)	ADMINISTRATIVE
COMPENSATION SCHEME FOR COMPLETION)	CASE NO. 323
OF INTRALATA CALLS BY INTEREXCHANGE)	PHASE I
CARRIERS, AND WATS JURISDICTIONALITY)	

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O R D E R

PROCEDURAL BACKGROUND

The Commission initiated this investigation on October 6, 1988 to review its determination that, though interLATA competition was in the public interest, intraLATA competition was not in the public interest.¹ The Order made all telephone utilities under the Commission's jurisdiction parties to this proceeding. To ensure that all aspects of intraLATA toll competition were addressed, the October 6, 1988 Order included an extensive data request. An informal conference was also held November 4, 1988 to discuss the issues listed in the Order initiating this investigation.

The Attorney General of the Commonwealth of Kentucky, by and through his Utility and Rate Intervention Division ("Attorney General"), was granted intervention on October 21, 1988. International Telecharge, Inc. and Kentucky Telephone Corporation were also granted intervention.

¹ Administrative Case No. 273, An Inquiry Into Inter- and IntraLATA Intrastate Competition in Toll and Related Services Markets in Kentucky, Orders dated May 25, 1984, October 26, 1984, and May 2, 1985.

Parties responded to the Commission's data requests in the October 6, 1988 Order concerning intraLATA competition (Phase I of this proceeding) on March 10, 1989. These responses were considered prefiled testimony. On March 10, 1989, there was filed a Joint Motion of a Coalition of Local Exchange Companies and Interexchange Carriers ("Joint Motion"). The coalition was comprised of all local exchange carriers ("LECs") except for South Central Bell Telephone Company ("South Central Bell") and included AT&T Communications of the South Central States, Inc. ("AT&T") and US Sprint Communications Company ("US Sprint").² The Joint Motion contained a plan for phasing in intraLATA competition, addressed revenue requirements and rate design issues, and proposed gradual introduction of competition excluding 1+ presubscription over a 2-year period. The Commission held an informal conference to discuss the Joint Motion on May 9, 1989.

By Order dated July 28, 1989, the Commission scheduled a hearing to address whether intraLATA competition was in the public interest, and stated that a separate hearing to address the Joint Motion would be scheduled upon the conclusion of the initial hearing. The Commission enumerated the issues that would be discussed at the public interest hearing in an Order dated November 27, 1989, stating that the hearing would include general

² Leslie County Telephone Company was granted permission to remove itself from the coalition of LECs and IXC's and file its own testimony concerning the Joint Motion on December 18, 1989.

questions concerning implementation of intraLATA competition, but would not include a discussion of advantages or disadvantages of any specific implementation options.

The public interest hearing convened on December 11, 1989 and was reconvened on January 10, 1990. Testimony was presented by AT&T; MCI Telecommunications Corporation ("MCI"); US Sprint; LDDS, Inc. ("LDDS"); AmeriCall Systems of Louisville ("AmeriCall"); Alltel Kentucky, Inc. ("Alltel"); Contel of Kentucky ("Contel"); Cincinnati Bell Telephone Company ("Cincinnati Bell"); GTE South Incorporated ("GTE South"); Independent Telephone Group ("Independent Group"); Leslie County Telephone Company ("Leslie County"); South Central Bell; and the Attorney General. Briefs were filed by AT&T, MCI, US Sprint, LDDS, AmeriCall, Alltel, GTE South, South Central Bell, and the Attorney General. Reply briefs were filed by AT&T, MCI, US Sprint, LDDS, South Central Bell, and the Attorney General.

On March 29, 1990, the Commission issued an Interim Order finding that a prima facie case exists that allowing intraLATA facilities-based toll competition would be in the public interest, and that such competition should extend to equal access on a presubscribed basis and include intraLATA interexchange private line service, intraLATA interexchange message toll services, and intraLATA interexchange operator services, with the implementation phase to proceed apace.

GTE South, Leslie County, and South Central Bell filed motions for rehearing. Cincinnati Bell filed a memo in support of

GTE South's motion; MCI and AT&T filed responses to the motions. On May 4, 1990, the Commission denied all motions for rehearing.

By Order dated May 24, 1990 the Commission established the issues to be addressed in the implementation portion of this proceeding, including an evaluation of the Joint Motion. On July 2, 1990, the coalition of LECs and interexchange carriers ("IXCs") filed a Supplement to the Joint Motion, which included the creation of an industry task force to address equal access and presubscription issues. Hearings on implementation of intraLATA competition commenced October 29, 1990. The following parties presented testimony: the Attorney General, AT&T, MCI, US Sprint, LDDS, Contel, Cincinnati Bell, GTE South, Independent Group, Alltel, and South Central Bell. Post-hearing briefs were filed by AT&T, MCI, US Sprint, LDDS, Alltel, Contel, GTE South, South Central Bell, and the Attorney General. Reply briefs were filed by AT&T, MCI, Alltel, and South Central Bell.

On December 7, 1990, the Commission requested parties to address the issue of whether the Commission could require that a portion of intraLATA toll traffic be returned to a LEC to expand the LEC's local calling area, even after the implementation of intraLATA competition. AT&T, MCI, US Sprint, Cincinnati Bell, and South Central Bell filed briefs in response to this request.

LEGAL ISSUES

The interim Order dated March 29, 1990 discusses federal and state law concerning the Commission's authority to make a

determination that intraLATA competition is in the public interest.³ The Commission found that it had the authority to authorize intraLATA competition based on Kentucky Utilities Co. v. Public Service Commission, Ky., 390 S.W.2d, 168, 174 (1965) which stated "[w]hether, in the overall public interest, competition has advantages that offset those of a monopoly is a question our legislature has chosen to leave to the decision of the Public Service Commission."

There remains the question regarding the need to expand a local calling area after the initiation of intraLATA toll competition. By Order dated December 7, 1990, the Commission requested briefs concerning the issue of its authority to return to the exclusive domain of the LEC a portion of intraLATA toll traffic. All parties responding agreed that this would not constitute confiscation with regard to any IXC that may have competed for the toll traffic. South Central Bell suggested that the Commission require competing carriers to waive any possible existing rights to that traffic where the Commission reasonably determines a local calling area should be expanded.⁴ However, a waiver is not necessary. The Commission's authority to require carriers to provide service in an economical manner and consistent with the public interest leaves it the option, after notice to carriers and a hearing on the merits, to revert to the exclusive

³ Order dated March 29, 1990, at pages 2-4.

⁴ Brief of South Central Bell, filed January 7, 1991, page 8.

service by a LEC of an area previously subject to toll competition.

INTRALATA COMPETITION

Benefits of Authorizing IntraLATA Competition

The parties' testimony supports the finding that intraLATA facilities-based toll competition is in the public interest. AT&T took the position that:

Under competitive market conditions, each firm, in its attempt to maximize its profits, is driven to: (1) charge a price equal to incremental costs; (2) charge the lowest price consistent with the long-run survivability of the industry; (3) service all customers willing to pay that price; (4) avoid discriminatory pricing or practices; and (5) introduce new products and cost-saving technological changes as rapidly as possible. Thus, where competition is present, the public interest is well-served by market forces. Consumers are provided quality services at low prices, and the overall economy benefits from introduction of the latest, most modern facilities and services.⁵

In addition to these benefits, MCI mentioned that competitive production of goods and services results in the most efficient use of inputs and allows society to spend less on regulatory programs. MCI cited several examples of actions the IXCs have taken to become more efficient.⁶ MCI also stated that "Limiting the interexchange carriers to the carriage of interLATA traffic will preclude efficient uses of their networks and deter optimal growth and changes to their networks."⁷

⁵ Testimony of Dr. David Kaserman, filed August 25, 1989, page 3.

⁶ Testimony of Dr. Nina Cornell, filed March 13, 1989, page 4.

⁷ Id., page 10.

MCI claimed that facilities investment would be long term, while marketing investment would be both short term and long term. In addition, marketing investments would be increased by authorizing 1+ presubscription.⁸ MCI added that authorization of entry will increase telecommunications investment in the rural areas because companies will respond to the increase in demand for equal access by rural customers. However, in MCI's opinion, true competition and the resultant benefits will occur only if the Commission deals with the bottleneck monopoly power of the LECs and, ultimately, with 1+ presubscription.⁹ MCI also claimed that if limited entry were authorized, services would be targeted toward business customers. However, with authorization of 1+ authority, MCI would be more likely to serve residential customers.¹⁰

US Sprint also agreed with AT&T and MCI concerning the benefits for consumers in authorizing intraLATA competition.¹¹ In addition, US Sprint claimed that by authorizing intraLATA competition the Commission would increase the size of the market which would be an incentive for IXC's to service rural areas.¹²

⁸ Transcript of Evidence ("T.E."), Volume III, pages 30-32.

⁹ T.E., Volume III, page 131.

¹⁰ T.E., Volume IV, page 6.

¹¹ T.E., Volume V, pages 91-94.

¹² T.E., Volume V, pages 83-84.

US Sprint stated that authorization of intraLATA competition "will have a positive effect on attracting and maintaining and preventing companies from leaving the state of Kentucky."¹³ However, US Sprint stated, "One-plus brings up a whole new set of problems and concerns. The competition faced by local exchange carriers would be higher under one-plus."¹⁴

Alltel¹⁵, Contel,¹⁶ Cincinnati Bell,¹⁷ GTE South,¹⁸ Independent Group,¹⁹ and Leslie County,²⁰ identified benefits similar to those described by AT&T, MCI, and US Sprint acknowledging that business customers benefit first, but that benefits accrue to residential customers as well.

It is important to note that the majority of the LECs, that have endorsed intraLATA competition and are signatories to the Joint Motion, conditioned their description of potential benefits with other issues that should be considered. These issues included local rate impacts, universal service, the continuation of geographically averaged toll rates and the need for a gradual

¹³ T.E., Volume V, page 85.

¹⁴ T.E., Volume V, page 80.

¹⁵ T.E., Volume IV, pages 214-215.

¹⁶ T.E., Volume IV, pages 235-236.

¹⁷ T.E., Volume IV, page 245.

¹⁸ T.E., Volume V, page 12.

¹⁹ T.E., Volume V, page 37.

²⁰ T.E., Volume V, page 61.

transition. GTE South indicated that LEC imputation requirements and dominant carrier status also needed to be addressed²¹

The Attorney General's proof reflected that all the witnesses in the proceeding are in agreement that at least some benefits will result from additional intraLATA entry. The question seems to be, "at what cost?"²² However, in response to a request for its assessment of the potential financial impact on the LECs in the intraLATA market if they were to lose 1+ authority, the Attorney General's witness testified:

That's the only aspect of Ms. Thompson's survey in my analysis, that we come to a similar conclusion, in that if we do eliminate the one-plus calling capability, at current rates there can be significant impact on the LECs. If the Commission is interested in moving in that direction, I think that it has got to give it a lot more thought, and address issues that haven't been addressed here.²³

In evaluating the benefits of intraLATA competition, South Central Bell's proof was that "competition in the intraLATA toll market should not be regarded as an obvious benefit. That's not to say it is not a benefit, but. . . -- its' got both costs and benefits."²⁴ For example, South Central Bell stated that competition might erode economies of scale, and regulatory costs will not be lower even if the market requires only partial regulation.

²¹ T.E., Volume V, page 7.

²² T.E., Volume VII, page 6.

²³ T.E., Volume V, page 60.

²⁴ T.E., Volume VIII, page 49.

South Central Bell acknowledged that although competition is not an obvious benefit, that fact alone doesn't mean it should not be pursued. South Central Bell's concern is that introduction of competition into a market with imbalanced rates will result in competitive entry that is not efficient. In concluding its discussion of the benefits of intraLATA competition, South Central Bell stated:

The problem here is not that the Commission is faced with dreadful choices or the choice between the lesser of evils, the Commission has lots of opportunities here. But it has to recognize that if it wants to engage in a competitive experiment that may have tremendous benefits in Kentucky, it has to set the ground work for that, and the ground work for that is to get rates more closely in line with the costs.²⁵

If you are arguing for facilities based competition, you can make a convincing argument that there are potential benefits to the citizens of Kentucky of having competing facilities based carriers. They are going to control each other's cost. They are going to serve as stimulus to -- each to the other to produce services better.²⁶

South Central Bell did not present any arguments to indicate that the benefits of competition, which have occurred in the interstate and interLATA markets, will not occur in the intraLATA market. Rather, South Central Bell emphasized the need for rate restructuring to result in an efficient and competitive intraLATA market.

In authorizing intraLATA competition, the Commission is relying heavily on its observations of the results of competitive

²⁵ T.E., Volume VIII, page 53.

²⁶ T.E., Volume IX, page 95.

activity in the interstate and interLATA markets. Most parties provided examples of the benefits that have accrued to consumers as a result of interstate and interLATA competition. Those benefits have included increased service offerings, technological innovation, and a decline in the price of services. All parties acknowledged that benefits will occur from authorization of intraLATA competition. However, they differ in their recommendations on the type and timing of regulatory changes which the Commission should implement to encourage the development of an efficient market.

To achieve the benefits that have occurred in interLATA markets in the intraLATA toll market, the Commission must permit a regulatory system that allows the development of an efficient market. Various parties have advocated different mechanisms to achieve an efficient marketplace.

Partially competitive markets are inherently inefficient. The unique characteristics of the intraLATA market further complicate designing a regulatory system that provides the maximum assistance in creating an efficient intraLATA toll market. Those unique characteristics include the local service obligation of the LECs, monopoly provisioning of access and federal court restrictions imposed on South Central Bell and GTE South. It is the Commission's desire to create a regulatory environment that will achieve the benefits of a competitive intraLATA toll market and ensure the provision of reliable, adequate local telephone service.

Inclusion of 1+ presubscription in the development of intraLATA competition will encourage the most efficient investment decisions by new entrants and maximize utilization of existing investment. The types of benefits which result from competition do not vary based on the extent of competition authorized. Rather, it is the cost and the amount of time required for the LECs and ultimately the ratepayers to absorb these costs--if they are not offset by other market forces--that vary.

If the Commission were to exclude 1+ presubscription, the result would be a short-lived interim step in creating competition in the intraLATA toll market. It would not provide the IXC's, resellers or the LECs the long-run policy direction needed to make appropriate investment decisions in Kentucky. Given the pace of technological change and the existing encroachment of IXC's into the intraLATA toll market, the 1+ presubscription issue must be included.

The original Joint Motion filed March 10, 1989 included a provision to initiate a review of further expansion of competition including 1+ presubscription 2 years after the effective date of the Phase I Order. This is rejected. A delay in authorizing 1+ presubscription will stifle the benefits of the Commission's finding that intraLATA competition is in the public interest. It will create an artificial boundary that would increase inefficiency in the development of a competitive intraLATA toll market. Authorization of competition in the full range of intraLATA toll services is in the public interest, will provide policy direction to the telecommunications industry, and maximize

the long-run benefits to the ratepayer. IntraLATA competition is viable and sustainable and local rates and universal service will not be significantly harmed.

A Task Force on 1+ presubscription will be established to compile and analyze detailed information on the implementation process. The scope of work of the Task Force is described in a subsequent section of this Order.

Viability and Sustainability of Competition

AT&T conducted a Kentucky Competitive Presence Survey. Competitive presence was defined primarily as the availability of competitive alternative carriers, other than AT&T, that can provide the service at a price that consumers are willing to pay.²⁷ Based on the survey, AT&T concluded that a competitive market for long-distance services in Kentucky is sustainable because the results demonstrate that Kentucky consumers are aware of and use services of other competitive firms.²⁸ To further support its position, AT&T also presented data indicating that a large number of firms purchase switched access nationally and in Kentucky.²⁹ AT&T filed data to describe the extensive intrastate transmission capacity, including private microwave systems and competitive alternatives, offered by other carriers in Kentucky.³⁰

²⁷ T.E., Volume I, page 164.

²⁸ Testimony of Neil Brown, filed August 25, 1989, page 10.

²⁹ Testimony of Don Ballard, filed August 25, 1989, pages 5-6.

³⁰ Testimony of Les Sather, filed August 25, 1989, pages 19-21.

AT&T stated that the amount of capital investment required to participate in a facilities-based intraLATA competitive market would not be a barrier to entry for other IXCs because some new companies could enter as non-vertically integrated firms, which would require little or no investment, and other firms could use their existing network in combination with purchasing access services from a LEC.³¹

MCI also claimed that effective competition exists in the interLATA market and noted the advanced technological changes that have occurred as a result of competition, as well as the increasingly procompetitive responses of AT&T to the price pressures confronting it from other companies.³² MCI also provided similar data on competing networks, services and changes in market share used by AT&T to support its conclusion that effective competition exists in the interstate and interLATA markets.³³ US Sprint claimed that the benefits to consumers from increases in competition in the interLATA market have clearly been demonstrated, and to support its argument, identified benefits similar to those advanced by AT&T and MCI.³⁴ LDDS claimed that consumer benefits, similar to those identified by AT&T, MCI, and US Sprint, have occurred as a result of interstate and interLATA

³¹ Testimony of Dr. David Kaserman, filed August 25, 1989, pages 132-134.

³² T.E., Volume III, page 65.

³³ MCI's Response to Commission Order dated October 6, 1988, page 5.

³⁴ T.E., Volume V, page 73.

competition.³⁵ The Attorney General also confirmed that effective interLATA competition is unfolding and will exist in the near future.³⁶

None of the parties filed information to dispute the fact that an effective, sustainable, competitive interLATA market in Kentucky is evolving. The Commission is convinced that the record in this case establishes that effective interLATA competition is evolving in Kentucky.

With regard to intraLATA competition, in Case Nos. 9874, 9902, 9928 and 10106,³⁷ the Commission granted conditional approval to several IXC interLATA service offerings provided by AT&T, MCI, and US Sprint which were capable of completing intraLATA traffic.³⁸ Data filed by the IXCs with the Commission on the sales of the intraLATA portion of these services indicate a growing demand. AT&T claimed that the level of sales from the incidental intraLATA traffic from its services such as MEGACOM, MEGACOM 800, Readyline, and others have already proven that there

³⁵ T.E., Volume VI, pages 146-148.

³⁶ T.E., Volume VII, page 11.

³⁷ Case No. 9874, AT&T Tariff Filing Proposing Megacom/Megacom 800 Service; Case No. 9902, US Sprint's Tariff Filing Proposing to Rename its WATS Products, Change Billing Calculations Methods for WATS, Introduce Ultra WATS, Travelcard, Direct 800, and Ultra 800; Case No. 9928, MCI's Tariff Filings to Establish Prism Plus, Prism I, and Prism II Services; Case No. 10106, AT&T Tariff Filing Proposing AT&T 800 Readyline.

³⁸ The incidental intraLATA traffic from these services is subject to compensation to the affected LEC in Phase II of this proceeding.

is a viable and sustainable, competitive intraLATA market. MCI confirmed AT&T's conclusions, citing the amount of its incidental intraLATA traffic from services such as Prism Plus, Prism I and Prism II.³⁹

LDDS described some of the intraLATA benefits that have already occurred as a result of the retail competition provided by resellers. LDDS attributed some of the stimulation of South Central Bell's growth in toll traffic to marketing activity by resellers. LDDS also stated that less quantifiable benefits of intraLATA competition are the merger of less efficient firms with stronger ones and increased efficiency in billing processes that work to promote a viable and sustainable market.⁴⁰ LDDS, moreover, claimed that the presence of resellers has expanded consumer choices and provided a greater variety of service configurations and pricing plans.⁴¹ Clearly, resellers have also established competitive niches in the intraLATA market.

Finally, all LECs except South Central Bell have, through their participation in the Joint Motion, acknowledged the movement of the telecommunications industry toward expanded competition in the intraLATA market. Although not a participant of the Joint Motion, South Central Bell provided information that indicates the demand for a competitive intraLATA market exists. Thus, the Commission concludes that sufficient evidence exists which shows a

³⁹ T.E., Volume III, pages 68-69.

⁴⁰ T.E., Volume VI, page 43.

⁴¹ T.E., Volume IV, page 78.

developing demand for competition in intraLATA service offerings and that competition in the intraLATA market will be viable, sustainable, and in the public interest.

Projected Impact on Local Rates and Universal Service

The Commission is convinced that a competitive intraLATA market is emerging, and notes that the rate of development has not seriously impacted the LECs. IntraLATA competition will not result in significantly higher local rates or an erosion of universal service.

AT&T stated:

It is highly unlikely that there will be any adverse effect on local rates or universal service whatsoever. This conclusion is based on four considerations. 1) On a theoretical level, the combination of market stimulation and access charges indicates that LEC revenues (and, therefore, the contribution to local rates) need not be harmed by entry. In fact, it is quite possible that LEC net revenues will increase; 2) Other states have allowed such entry without experiencing such adverse consequences; 3) The Kentucky Commission has already allowed intraLATA toll entry by resellers, and local rates have not been driven up by a loss of revenue flow to the LECs. There is no reason to expect the outcome to be any different once facility-based entry is allowed; and 4) The Joint Motion that has been filed in this docket provides a safeguard that effectively guards against any undesired effects on local rates or universal service.⁴²

MCI agreed with AT&T's overall assessment that local rates and universal service will not be adversely affected. MCI does not believe entering IXCs will capture a large share of the market

⁴² Testimony of Dr. David Kaserman, filed August 25, 1989, page 33.

and, moreover, those carriers will have to purchase access services from the LECs.⁴³

As empirical evidence, AT&T presented the results of three separate papers using econometric models to estimate the magnitude and statistical significance of the changes in toll prices that are forecasted to occur from an open entry policy. After summarizing the studies, AT&T concluded:

The available evidence shows that neither the BOC nor the local ratepayer are harmed by allowing facility-based intraLATA competition. Therefore, the benefits experienced by toll users are not offset by any costs imposed on local users. As a result, an open entry policy is unambiguously in the public interest.⁴⁴

AT&T did acknowledge that the empirical evidence presented was far from perfect; however, it was AT&T's opinion that the evidence indicated no adverse effect on LEC revenues, universal service or local rates.⁴⁵ US Sprint drew similar conclusions from the empirical studies.⁴⁶

AT&T reiterated that the stimulation in toll traffic, which will occur as a result of the decrease in toll prices, will result in an increase in access revenue partially offsetting the LEC's revenue loss from toll rate reductions and mitigating an increase in local rates. AT&T concluded that, based on evidence from other states, a revenue loss for the LECs won't occur. AT&T also stated

⁴³ Testimony of Dr. Nina Cornell, filed March 13, 1989, page 12.

⁴⁴ Testimony of Dr. David Kaserman, filed August 25, 1989, page 37.

⁴⁵ T.E., Volume II, page 47

⁴⁶ T.E., Volume V, page 74.

that the demand for long-distance telecommunications is growing approximately 10 percent a year.⁴⁷

AT&T's proof also showed that existing intraLATA competition from resellers and IXC authorized intraLATA services has not adversely impacted LECs' revenues due to the growth in minutes of intraLATA toll and interLATA access since 1985⁴⁸ and that no LEC has demonstrated any financial harm from competitive services in the intraLATA market during this same period.⁴⁹ AT&T stated that its goal is to support universal service by paying its fair share of the cost of connection via access charges to the LECs.⁵⁰

With regard to changes in LEC market share resulting from the introduction of intraLATA competition, MCI predicted that the process will be the same as in the early days of entry in the interstate market with the incumbent firm maintaining an enormous market share.⁵¹ Thus, in MCI's opinion, the LEC's revenues will not be jeopardized. MCI believes that since the LECs have the most incentive to bring forth evidence of a negative impact from intraLATA competition in states allowing intraLATA competition and have not done so, that significant damage must not be occurring.⁵²

⁴⁷ T.E., Volume II, pages 42-44.

⁴⁸ Response of AT&T to PSC Order dated October 6, 1988.

⁴⁹ T.E., Volume II, page 161.

⁵⁰ T.E., Volume I, page 61.

⁵¹ T.E., Volume III, page 125.

⁵² T.E., Volume III, pages 78-79.

All the LECs that are signatories to the Joint Motion claimed that the impact of authorizing intraLATA competition on local rates and universal service will be minimal if the terms of the Joint Motion are adopted. Although several signatories acknowledged that there are other ways to introduce intraLATA competition, without specific details and terms, they could not predict the impact on local rates or universal service. GTE South, moreover, claimed that although it did not expect stranded facilities if intraLATA competition was authorized in accordance with the Joint Motion, it did expect some underuse of facilities.⁵³

The Attorney General concluded that the negative financial effects on the LECs are likely to be nonexistent or quite small if the LECs retain 1+ exclusivity. This conclusion, assembled from studies and analysis from other jurisdictions, is based on three factors: 1) the LECs are likely to retain a large share of the toll business particularly if there is no intraLATA equal access; 2) to the extent that the LECs lose market share, the IXCs that gain toll volume will have to take access service from the LECs; and 3) the LECs will also benefit from market stimulation due to competition.⁵⁴

South Central Bell claimed that in 1989, the intraLATA competition already authorized by the Federal Communications Commission ("FCC") and by this Commission has resulted in a

⁵³ T.E., Volume V, page 10.

⁵⁴ T.E., Volume VII, pages 7-8.

conservative estimated revenue loss of approximately \$10 million.⁵⁵ In evaluating South Central Bell's \$10 million loss estimate from current competition, the Commission notes the conclusions of the Theodore Barry and Associates ("TB&A") Incentive Regulation Plan Review.⁵⁶ TB&A stated:

Despite significant growth in facility bypass reported to the FCC, SCBK's market share remains high and any existing threat to its revenue base is minor, therefore not materially affecting general ratepayers.

South Central Bell also filed a Contribution Loss Study to determine what impact further competition would have. To develop the Contribution Loss Study, South Central Bell conducted a Market Research Survey to estimate how many customers would choose alternate companies to provide their long-distance service. South Central Bell used this data to project market share changes and the resulting contribution loss. The Study concluded that if intraLATA facility-based competition on a 10XXX basis was permitted in Kentucky, at 1989 revenue and traffic levels, an annual contribution loss of \$22 million would result. If South Central Bell also lost the remaining right to 1+/0+ exclusivity within the LATA, South Central Bell maintained that the losses would be even greater at approximately \$31 million in contribution.⁵⁷ South Central Bell concluded that customers will

⁵⁵ T.E., Volume VIII, page 121.

⁵⁶ TB&A Incentive Regulation Plan Review Report, filed in Case No. 90-256 on September 4, 1990, page XI-12. This Plan Review was introduced in its entirety in this case by South Central Bell.

⁵⁷ T.E., Volume VIII, page 122.

leave the company because they prefer the simplicity and ease of having one carrier to complete all their long-distance calling and because competitors will be able to offer lower prices.

The Commission has thoroughly reviewed the results of the Market Research Survey filed by South Central Bell which formed the basis of its conclusions for the residential and business segments. Certainly the Commission accepts the basic premise that with the introduction of competition, South Central Bell's market share, by segment, will change. However, the survey has flaws. In developing its estimates, South Central Bell assumed a flash cut for customer conversion to other companies. The flash-cut assumption means that those customers who convert from South Central Bell to another carrier would do so simultaneously. The use of the flash-cut assumption is not realistic, a defect South Central Bell acknowledged.⁵⁸ Data obtained on changes in market share in other states that have authorized intraLATA competition does not support the assumption of a flash-cut conversion but rather a gradual shift. A gradual shift will provide adequate time for South Central Bell and other LECs to respond to the changing markets.

The survey also did not make any provision for the impact on customer choice if South Central Bell's toll pricing structure changed. South Central Bell, however, acknowledged that some of its survey results indicated that the demand for its toll services, given intraLATA competition, will be dependent on its

⁵⁸ T.E., Volume VIII, page 79.

toll prices.⁵⁹ Yet, despite this knowledge, the Contribution Loss Study failed to factor in toll price changes and stimulation in its loss estimates. It is also noteworthy that South Central Bell, in Case No. 90-256⁶⁰ pending before this Commission, has requested reductions in toll and access prices.

South Central Bell stated that the effect of traffic stimulation was not included in the contribution loss estimates because of the difficulty of determining the price reduction necessary for competitors to attract customers from the LECs, the difficulty of predicting other marketing effects, and the fact that the Commission has not recognized stimulation in demand in past rate cases.⁶¹ The Commission notes that since South Central Bell's contribution loss estimates did not recognize the increase in demand for toll, the estimates did not reflect an increase in demand for access which would accrue as a result.

South Central Bell described how the Modified Final Judgment ("MFJ") LATA constraints would place it at a competitive disadvantage. Resellers and IXC's could create a complete package of service offerings statewide or nationally to meet a customer's total needs while South Central Bell could not. South Central Bell argued that the current differential between access rates and

⁵⁹ T.E., Volume VIII, page 136.

⁶⁰ Case No. 90-256, A Review of the Rates and Charges and Incentive Regulation Plan of South Central Bell Telephone Company.

⁶¹ T.E., Volume VIII, page 127.

toll rates is not cost based and that this differential will necessitate local rate increases if not corrected.

The Commission is aware of the potentially adverse effect on South Central Bell as a result of the restrictions against offering service outside the LATA. However, as South Central Bell acknowledged, resolution of this issue is beyond this Commission's jurisdiction.⁶² Although there may be some additional risk to South Central Bell's revenues as a result of this restriction, the effect should not be substantial. The benefits of competition outweigh this disadvantage.

South Central Bell presented evidence concerning New York Telephone and the adverse impact intraLATA competition has had on that company's finances and its local rates. South Central Bell claimed that facilities and service bypass were occurring in New York Telephone's service area and that it would be a mistake to assume that facilities-based bypass is not possible in Kentucky.⁶³ However, South Central Bell's proof also reflected that there is not a clear empirical record on which to judge competition in telecommunications.⁶⁴

The record supports the conclusion that changes in market share from intraLATA facilities-based competition will occur gradually. The Commission is convinced that the market stimulation and the increase in demand for access will be mitigating

⁶² T.E., Volume VII, page 112.

⁶³ Id.

⁶⁴ T.E., Volume VIII, page 98.

factors in reducing the possible negative impact on local rates and universal service resulting from intraLATA competition. Rate rebalancing may be necessary for the LECs to effectively compete. Given a reasonable plan of implementation, local rates and the revenues of LECs will not be significantly changed. Thus, the Commission's goal of universal service will not be adversely affected. Moreover, many of the benefits of competition may actually help reduce customers' total telephone bills.

IMPLEMENTATION

The Joint Motion

On March 10, 1989, a coalition of LECs⁶⁵ and IXC⁶⁶s filed a Joint Motion moving the Commission to adopt an intraLATA competition implementation plan and a method for managing non-traffic sensitive revenue requirement allocation to toll services. The coalition filed a supplement to the Joint Motion on July 2, 1990. The supplement provided additional information on activities that must occur to accomplish the objectives of the Commission's March 29, 1990 Interim Order.

The coalition represents the Joint Motion as a mechanism that would allow a scheduled implementation of intraLATA competition while, at the same time, ensuring that non-traffic sensitive revenue derived from toll services is not diminished.⁶⁷

⁶⁵ All LECs except South Central Bell.

⁶⁶ AT&T and US Sprint.

⁶⁷ Joint Motion, filed March 10, 1989, page 2.

Conceptually, the coalition plan for non-traffic sensitive revenue management is an expansion of the ULAS⁶⁸ concept. As with ULAS, the non-traffic sensitive requirement applicable to toll services would be determined and administered uniquely for each LEC. However, unlike ULAS, the coalition plan incorporates both an interLATA and intraLATA non-traffic sensitive requirement. The combined non-traffic sensitive requirement would be recovered individually by each LEC from toll service providers serving its operating area, including the intraLATA pool, resellers, and other purchasers of switched access services, based on each access user's terminating minutes of use.⁶⁹

According to the coalition, the Joint Motion is designed to accomplish the following objectives:⁷⁰ (1) a scheduled implementation of intraLATA competition; (2) ensure that intraLATA competition does not cause upward pressure on local exchange rates or interLATA and intraLATA toll rates, except as may be unavoidable to equalize the per unit non-traffic sensitive contribution among toll carriers; (3) provide the Commission with a mechanism to establish and monitor the non-traffic sensitive requirement applicable to toll services and the revenue flowing to each LEC, without affecting the revenue flowing to any other LEC, through setting a non-traffic sensitive revenue requirement per access line; and (4) promote the concept of universal service.

⁶⁸ Universal Local Access Service.

⁶⁹ Joint Motion, filed March 10, 1989, page 2.

⁷⁰ Id., page 3.

The plan for non-traffic sensitive revenue management is designed to apply where toll services provided by LECs are handled either through a pool arrangement or in a non-pooled environment, and accommodates the provision of toll services by an individual LEC in its market area. Therefore, there are no provisions in the plan that would require changes to existing intraLATA pool participation, structural changes to the operation of the existing intraLATA pool, or changes to the provision of toll services by LECs that do not participate in the existing intraLATA pool.⁷¹

The Joint Motion states that it is based on the following principles:⁷²

(1) Initially, the non-traffic sensitive revenue derived from the aggregate of intrastate toll services should be computed for each LEC based on formulas specified in the Joint Motion. The formula yields a revenue neutral result. Subsequently, the annual non-traffic sensitive requirement should be computed for each LEC based on the number of access lines in service and the tariffed non-traffic sensitive recovery rate per access line. This allows non-traffic sensitive revenue to grow as a function of access line growth.

(2) Non-traffic sensitive revenue derived from interLATA and intraLATA toll services should be the same per unit of traffic and should not vary with minutes of use.

⁷¹ Id., pages 3-4.

⁷² Id., pages 4-5.

(3) At the starting point, each LEC should compute its non-traffic sensitive requirement per access line per month as specified in the motion and file the resulting rate with the Commission as part of its intrastate access services tariff.

(4) As used in the plan, intraLATA traffic sensitive elements include all intraLATA settlement elements except network compensation, billing and collection settlements, carrier common line charges, and residual disbursements.

(5) Non-traffic sensitive recovery should be based on terminating minutes of use. Billing by LECs to access users should be based on either each access user's relative percentage of total minutes of use, or a rate per minute of use designed to recover the authorized non-traffic sensitive rates in the future by mirroring interstate tariffed rates, or by documenting proposed changes with an intrastate-specific cost-of-service study.

Mathematically, the formula for determining the initial non-traffic sensitive revenue requirement applicable to toll services is relatively simple. Essentially, it is the sum of interLATA and intraLATA carrier common line revenue, ULAS revenue, and the revenue impact of changing interLATA access services rates and intraLATA toll settlement rates to mirror current interstate access services rates.⁷³ Likewise, translation of the total non-traffic sensitive requirement into meaningful rates and charges is relatively simple.⁷⁴

⁷³ Id., Appendix A.

⁷⁴ Id., Appendix B.

The coalition proposes a three step phase-in of intraLATA competition. Initially, intraLATA competition would consist of approval on a permanent basis of IXC service offerings currently allowed on a conditional basis and the unblocking of "10XXX" carrier access code dialing.⁷⁵ Examples of IXC service offerings allowed on a conditional basis are AT&T Megacom, MCI Prism, and US Sprint UltraWATS. To implement this phase consistent with the Joint Motion, LECs would be required to change access services tariffs to reflect non-traffic sensitive revenue requirement applicable to toll services, billing procedures, and current interstate traffic sensitive rates or intrastate-specific traffic sensitive rates.⁷⁶ The coalition suggests that these tariff changes be made effective 60 days following a final decision in this phase of the proceeding, and that the ULAS tariff be canceled at the same time. In addition, coincident with the effective date of the stipulated tariff changes, LECs would be required to change intraLATA pool settlement rates and initiate service orders that permit 10XXX intraLATA traffic to be routed to IXCs. No tariff or rate changes would be required of IXCs.

Six months following a final decision in this phase of the proceeding, the coalition proposes to expand intraLATA competition to allow IXCs to provide intraLATA private line services and statewide WATS and 800 services.⁷⁷ In order to implement this

⁷⁵ Id., Appendix C, pages 1-2.

⁷⁶ Supplement to the Joint Motion, filed July 2, 1990, pages 2-4.

⁷⁷ Joint Motion, filed March 10, 1989, Appendix C, page 2.

phase, LECs would be required to change access services tariffs to allow IXC use of special access in the provision of intraLATA private line services, and modify the intrastate 800 database to allow statewide 800 service by IXCs.⁷⁸ Also, at their option, IXCs could make tariff changes removing restrictions on the provision of intraLATA private line services and statewide WATS and/or 800 services.

Finally, two years following a final decision in this proceeding, the coalition proposes that the Commission review further expansion of intraLATA competition, including 1+ presubscription.⁷⁹ In the interim, the coalition suggests that the Commission create an industry task force to examine the feasibility of 1+ presubscription.⁸⁰

South Central Bell, a non-signatory, expressed considerable opposition to the Joint Motion, largely on the grounds that it would allow intraLATA competition prior to the completion of a rate rebalancing program. South Central Bell proposed a rate rebalancing plan that deferred intraLATA competition for four years. South Central Bell's estimates of required revenue shifts were based on its market share research with which the Commission disagrees. MCI, also a non-signatory, expressed conditional

⁷⁸ Supplement to the Joint Motion, filed July 2, 1990, pages 4-5.

⁷⁹ Joint Motion, filed March 10, 1989, Appendix C, page 2.

⁸⁰ Supplement to the Joint Motion, filed July 2, 1990, pages 5-6.

agreement with the Joint Motion.⁸¹ All other non-signatory parties took essentially ambivalent positions on the Joint Motion.

The Commission finds that the Joint Motion as supplemented, which is attached hereto and incorporated herein, with the modifications discussed below is reasonable and should be approved. The Joint Motion as modified herein will provide an orderly transition to implement competition within the LATA.

The Commission's modifications to the Joint Motion are as follows:

First, while the Joint Motion specifies the initial establishment of non-traffic sensitive requirement and allows related revenue to grow as a function of access line growth, it does not explicitly address changes in non-traffic sensitive cost. None of the signatory parties that addressed this issue had any objection to the understanding that non-traffic sensitive requirements should be allowed to change as non-traffic sensitive cost changes. This understanding should be incorporated into the Joint Motion.

Second, the Joint Motion assumes a revenue neutral intrastate implementation of current interstate switched and special access services rates at the starting point. It is silent regarding future intrastate mirroring of interstate access services rates.

⁸¹ Response of MCI Telecommunications Corporation filed May 4, 1989 to the Joint Motion, filed March 10, 1989.

As in other cases,⁸² the Commission will not allow automatic mirroring, due to potential impact on overall revenue requirements. Instead, prospective access services tariff filings will be reviewed on their own merits. Also, the proposed revenue neutral implementation is a reasonable and practical plan that avoids immediate revenue dislocations that might result in local exchange rate increases. Therefore, the Commission will allow it.

Third, the Joint Motion provides for two methods of recovering non-traffic sensitive requirements. LEC billing may be based on each access user's percentage of total terminating minutes or based on a rate per access minute applicable to terminating minutes of use. The latter plan would require annual true-ups. It is also preferred by LECs.

The Commission will allow the use of either billing option, even though non-traffic sensitive cost should be recovered on a flat rate basis. The LECs will have to balance perceived administrative ease with the likelihood of bypass behavior when they select a billing option.

Fourth, as a result of the Joint Motion, intraLATA toll pool settlement rates will change. Revised settlement contracts should be filed with the Commission for review and approval. In addition, further residual settlements should cease upon initial

⁸² Case No. 8838, An Investigation of Toll and Access Charge Pricing and Toll Settlement Agreements for Telephone Utilities Pursuant to Changes to be Effective January 1, 1984.

implementation of the Joint Motion and accumulated residual funds should be targeted to intraLATA toll rate reductions, pending any further order of the Commission restoring residual settlements. This action will prevent the LECs from realizing any revenue windfall as a result of the implementation of the Joint Motion.

Finally, on the matter of timing, the coalition proposes that the initial phase of intraLATA competition should begin 60 days following a final decision in this phase. The Commission finds that this schedule is a bit overly ambitious, as among the tasks to be accomplished are the filing by LECs of revised access services tariffs that may be contested and which must be reviewed and approved by the Commission. A more reasonable schedule for implementing the initial phase of intraLATA competition is as follows: 30 days after the date of this Order, LECs shall file revised access services tariffs and revised intraLATA toll pool settlement agreements, and the initial phase of intraLATA competition shall commence 30 days following approval of the revised tariffs and settlement agreements. In any case, the initial phase will commence no later than 7 months from the filing date of the revised access services tariffs and settlement agreements.

Thirty days after the start of the initial phase of intraLATA competition, LECs shall file such additional tariff changes as are necessary to implement the second phase and certify a timetable for 800 database changes. The second phase of intraLATA competition shall commence 30 days following approval of the

additional tariff and database changes. In any case, the second phase of intraLATA competition will commence no later than 7 months following the filing date of required tariff revisions and 800 database conversion timetable.

IntraLATA Presubscription Task Force

The coalition of LECs and IXC's proposed that the Commission establish an industry task force to examine issues regarding intraLATA equal access and 1+ presubscription. Specifically, the coalition suggested that the task force examine:

1. The various methods of implementing 1+ pre-subscription and the technical availability of switching generics to achieve the various methods of implementation together with the cost of each.
2. The potential market changes resulting from 1+ presubscription.⁸³

Alternatively, South Central Bell contends that intraLATA equal access on a 1+ presubscribed basis should not be allowed prior to MFJ relief--specifically the removal of LATA boundaries. This argument has been earlier addressed and rejected.

The Commission agrees with the coalition that an industry task force should be created to examine the availability of switching equipment and software generics necessary to the implementation of intraLATA equal access and 1+ presubscription. The mission of the task force should be fact finding in nature. Its mission should not include evaluation of the possible financial impacts of intraLATA competition or market changes that

⁸³ Supplement to the Joint Motion, filed July 2, 1991, pages 5-6.

might result from intraLATA competition, as suggested by some parties.⁸⁴ Its mission should also not include the preparation of an implementation plan, although implementation options may be considered and offered for descriptive purposes. Hopefully, an emphasis on fact finding and fully explained alternatives will remove any pressure to produce a report representing a consensus of the participants. Once a task force report is prepared, interested parties will be accorded the opportunity to make individual recommendations concerning the implementation of task force findings.

Among matters the task force should consider are:

1. Specification of access features necessary to provide intraLATA equal access.
2. The availability and cost of intraLATA equal access software generics.
3. The relative merits and cost of generic upgrades to existing switching equipment and replacement alternatives for LECs planning central office or toll/access tandem change-outs in the normal course of business.
4. The relative merits and cost of requiring LECs to include intraLATA equal access capability with any installation of interLATA equal access generics.
5. The need for national protocol standards, including whether vendor-designed protocols vary or are likely to vary

⁸⁴ For example, Comments of Cincinnati Bell Telephone Company, filed July 13, 1990, Item 1.

substantially and whether national standards are likely to follow rather than precede state implementation.

6. The relative merits of alternative intraLATA equal access cost recovery mechanisms.

7. The relative merits and cost of alternative presubscription balloting procedures.

8. The need for any network reconfiguration to facilitate intraLATA equal access, including the relative merits and cost of centralized access tandems shared by groups of LECs.

9. The relative merits and cost of alternative intraLATA equal access implementation schedules.

The above list is intended to be illustrative but not exhaustive. Other items may be added as appropriate to produce a complete report, so long as additional items focus on technical matters incidental to intraLATA equal access and 1+ presubscription. The Commission does not intend for the task force to become a forum for re-arguing positions taken in this investigation or reevaluating decisions that have been made. To the extent that any participant has a grievance concerning the scope of the task force's mission or specific topics on the task force's agenda, these grievances should be brought before the Commission in the form of written pleadings.

LECs and other participants are required to be forthcoming in providing such information as may be needed by the task force. The Commission encourages the formation of technical subcommittees to deal with particular issues. Subsequent to an initial organizational conference, at which specific topics for inquiry

should be formulated and subcommittees assigned, the task force will submit a timetable for completion of its work. It is suggested that the task force's work proceed in stages. For example, it appears that the first task that must be accomplished is the specification of access features necessary to intraLATA equal access and the solicitation of information from switch manufacturers. Work stages should reflect logical progressions, but should not be used to preclude timely consideration of issues that can be dealt with concurrently. To the extent that a Commission ruling is needed after completion of any particular stage, the participants can petition for any indicated rulings.

We expect a presentation of factual information and descriptive alternatives relevant to intraLATA equal access implementation. Any actual implementation plan will be adopted by the Commission after the task force report is filed and individual comments made.

The Joint Motion stipulates that two years following a final decision in this investigation "the Commission will review further expansion of competition into the intraLATA market including presubscribed 1+ DDD calling."⁸⁵ MCI argues that the task force should complete its work within one year. The Minnesota project took approximately 18 months. The Commission encourages the task force to complete its work as expeditiously as possible, but does not wish to impose an unreasonable deadline. Given the Minnesota experience, the Commission will expect a finished report within 18

⁸⁵ Joint Motion, Appendix C, page 2.

months of a final decision in this phase of this proceeding and strongly encourages a faster paced schedule.

All parties to this proceeding shall be considered members of the task force. The Commission's Staff will coordinate and monitor the work of the task force.

Dominant Vs. Non-Dominant Carriers

In determining the degree of regulation of intraLATA market participants, we move to a discussion of dominant and non-dominant carriers. The parties were given two opportunities to present their position on the designation of dominant and non-dominant carriers in the intraLATA market. In doing so, they were asked to elaborate on the appropriate criteria to determine intraLATA market power and to make recommendations on the regulatory requirements that should apply to each category.

AT&T filed extensive testimony opposing designation of IXC's as dominant carriers in the intraLATA market. AT&T first presented arguments to support its conclusion that effective competition exists in the interLATA market and thus it should no longer be designated a dominant carrier in that market. AT&T concluded that the same arguments are relevant to the intraLATA market and the same conclusion should be drawn.

AT&T specifically noted that it currently has a small share of the intraLATA toll market based on the incidental intraLATA traffic from its MEGACOM, MEGACOM 800, and other services. In AT&T's opinion, South Central Bell will continue to maintain the bulk of the intraLATA toll market prospectively due to South Central Bell's network configuration which is designed to

efficiently handle the shorter distance calls associated with intraLATA toll and its regulatory-mandated right to all 1+ intraLATA traffic.⁸⁶ In addition, after existing regulatory barriers to entry are removed, it is AT&T's position that there will be nothing it can do to prevent new entrants from bringing increased supply to this market if prices should rise above competitive levels. Finally, as stated, AT&T claims the same characteristics exist in the intraLATA toll market that exist in the interLATA toll market--skewness of demand and a healthy growth rate in demand--that intensify competitiveness in the intraLATA market.⁸⁷ AT&T concluded, that for the same reasons, the other IXCs will not possess market power and should be unregulated in the intraLATA market.⁸⁸

However, with regard to South Central Bell, AT&T argues that due to South Central Bell's monopoly over access to the local network, it should be fully regulated. AT&T recommended a policy involving unbundling of services and imputation of access costs by the LECs to prevent such behavior.

MCI stated that the two tier scheme of regulation established by the Commission in Administrative Case No. 273 has worked smoothly and efficiently for it. MCI recommended the system be

⁸⁶ Prefiled Testimony of David L. Kaserman, dated August 25, 1989, page 25.

⁸⁷ Id.

⁸⁸ Prefiled Testimony of David L. Kaserman, dated August 25, 1989, page 28.

expanded into the intraLATA market. In MCI's opinion, LECs should be considered dominant carriers.⁸⁹

US Sprint took the position that as long as the LECs are the only carriers allowed to carry intraLATA traffic on a 1+ basis, they should be considered dominant carriers in their service areas. In addition, US Sprint thinks the same general set of rate justification rules that currently apply to AT&T in the interLATA market should also apply to the LECs in the intraLATA market. US Sprint also thinks LECs should be required to impute access charges in establishing their intraLATA toll rates.⁹⁰

LDDS stated that the LECs and AT&T should be regulated as dominant carriers. In LDDS's opinion the LECs enjoy a virtual monopoly in the intraLATA wholesale market.⁹¹ It is LDDS's position that, if not subject to dominant carrier regulation, the LECs will be able to use their power to engage in anti-competitive pricing strategies that would significantly hamper the development of effective and sustainable intraLATA competition. In addition, LDDS states that the LECs enjoy name recognition, visibility and good will, making it difficult to encourage customers to make a change.

AT&T should also be regulated as a dominant carrier in LDDS's opinion because AT&T can leverage its dominant interLATA position

⁸⁹ MCI's Response to Commission Order dated October 6, 1988, page 24.

⁹⁰ US Sprint's Response to Commission Order dated October 6, 1988, page 7.

⁹¹ Brief of LDDS, dated December 20, 1990, page 29.

to its advantage in the intraLATA market. LDDS also stated that AT&T also might engage in cost misallocations and other activities that would subvert the Commission's intent to regulate its interLATA operations.⁹² LDDS concludes that all other competitors in the intraLATA market should be designated as non-dominant carriers and be subject to the same regulatory standards as applied to non-dominant carriers in the interLATA market.

The Attorney General recommended that there be no change in the regulatory requirements for any intraLATA carrier at this time.⁹³ The Attorney General concludes that opening the intraLATA market to competition should not result in a change in the regulation of the LECs. The Attorney General's recommendation was based on the conclusion that opening the intraLATA toll market to competition absent the realization of intraLATA equal access, promises no change in structure or operations of the market and, therefore, should not be the source of any change in regulatory requirements.⁹⁴

All the LECs opposed designation as dominant carriers. Several LECs stated that, if intraLATA competition is authorized, LECs should be given the same flexibility as other competitors. They also indicated that regulatory requirements for all participants should be the same.

⁹² Id., page 31.

⁹³ Attorney General's Additional Direct Testimony, filed July 13, 1990, page 14.

⁹⁴ Id.

South Central Bell stated designation as a dominant carrier will be especially onerous for it due to the MFJ restrictions excluding it from the interLATA market. GTE South, which is also under restrictions in the interLATA market, expressed the same opinion for its operations. These carriers further argued that dominant status will also distort the competitive process causing uneconomical investment. South Central Bell also argued that the Commission's "willing and able" conditions for a competitive market, as established in Administrative Case No. 273, have been met as evidenced by its market research and AT&T's capacity study.⁹⁵ Finally, South Central Bell stated Commission scrutiny of entrants into the intraLATA market will preclude the occurrence of anti-competitive activities.

In evaluating the positions of the parties on this issue, the Commission has carefully reviewed the basis for its decision in Administrative Case No. 273, which established dominant and non-dominant carrier classifications in the interLATA market. In Administrative Case No. 273, the Commission identified four conditions that must be met to guarantee that market power cannot be exercised by a carrier. Those conditions were:

1. Consumers must be willing to switch suppliers in response to price changes.
2. Competing carriers must be willing to expand to meet the increased demand for their services that will be generated if another carrier raises its prices to an inefficiently high level.

⁹⁵ South Central Bell's Response to Commission Order dated May 24, 1990, Item No. 15.

3. Customers must be able to switch suppliers.

4. Competing carriers must be able to expand to meet increased demand.⁹⁶

Until the implementation of intraLATA 1+ presubscription occurs and a sufficient number of consumers use alternate carriers, these conditions will not be met to a sufficient degree to guarantee that market power cannot be exercised by the LECs.

Three conditions currently must be met for consumers to be able to use alternative carriers. The IXC or reseller must serve the customer's area, the serving offices must have touch tone capability, and the customer must have a touch tone telephone, or its equivalent. These conditions are not currently met for a sizeable number of Kentucky's citizens. Even after implementation of 1+ presubscription and expansion by the IXCs, there may be Kentucky residents who will have no alternative to the LECs for intraLATA toll service.

With respect to the supply side, the fact that it will take the IXCs time to expand their capacity to meet increased demand would make it possible for the LECs to exercise market power in the short term. Although the LECs will undoubtedly face significant competition on selected high traffic intraLATA routes, the majority of intrastate intraLATA routes will likely continue to be served by only one supplier. Even though the IXCs will

⁹⁶ Administrative Case No. 273, Order dated May 25, 1984.

purchase access services from the LECs, the monopoly position of the LECs on many routes will continue for some time. It will be physically possible for the IXC's to provide facilities-based service over only a small portion of the total intraLATA routes in the near future. It takes time to acquire rights-of-way, acquire property on which to construct facilities, construct buildings, put up microwave towers and other facilities, and install switching and other equipment. In addition, the IXC's will need time to educate the public and market their services.

The concept of market share typically figures prominently in any discussion of monopoly or market power. This measure has had a long history of development and utilization in both theoretical and applied economics. The FCC relied in part upon this concept in its determinations concerning dominant and non-dominant firms, and its findings that differing regulatory treatment should be accorded firms in these two categories. This concept is as appropriate in the intraLATA market as in the interLATA market. None of the LECs opposed designation as dominant carriers due to their low market share. Rather, the LECs argued for a level playing field with the new entrants to the intraLATA market. Although the Commission acknowledges that the IXC's and the resellers are acquiring market share, the vast share of the traffic remains with the LECs.

If full rate of return regulation of the LECs and the Commission's policy of requiring geographically averaged toll rates were changed at this time, the LECs would have the opportunity to

significantly raise toll prices and meet little or no competition on the bulk of their intraLATA routes. Moreover, the LECs would also have the opportunity to reduce toll prices on high density routes to less than competitive levels and increase the monopoly local rates to retain their overall earnings requirements. It is obvious that the Commission cannot expose the citizens of Kentucky to the potential abuse that could result from such a decision. It is simply incorrect to assert that the LECs do not possess significant market power in intraLATA toll in Kentucky at this time. In addition, the LECs must continue to be subject to full rate of return regulation due to their provisioning of access, a monopoly service.

Based on existing market share within the LATA, AT&T could not be considered a dominant carrier. However, the determination of whether AT&T is a dominant carrier within the LATA's should not be based on existing intraLATA market share, but rather on the ease with which AT&T can expand its operations and marketing program into the LATA, thereby posing a serious threat to the continued utilization of the LEC network by high volume customers. In addition, although AT&T has argued that the interLATA market in Kentucky is fully competitive, the Commission has only concluded that a competitive interLATA market is evolving. Many of the competitive advantages that AT&T has in the interLATA market will carry over into the intraLATA market.

AT&T also has a petition before the Commission requesting reduced regulation for intrastate operations in Case No. 90-431.⁹⁷ To ensure consistent regulation, the Commission has determined that AT&T should be subject to the same regulatory treatment in the intraLATA market as in the interLATA market, at least until this petition is addressed.

For these reasons, the Commission designates all LECs and AT&T as dominant carriers in the intraLATA market.

Imputation of Access Charges to IntraLATA Toll

AT&T, MCI, and other parties contend that the LECs should be required to impute access charges in pricing intraLATA toll services. It is their belief that imputation is necessary to prevent the LECs from obtaining an unfair price advantage vis-a-vis other toll carriers. The LECs did not take a direct position on the imputation issue.

In Case No. 9889,⁹⁸ the Commission allowed AT&T to reduce toll charges subject to the condition that no toll rate could be reduced below variable cost. Variable cost was defined in terms of access charges - specifically, carrier common line charges, traffic sensitive rates, and billing and collection charges. The same standard should apply to South Central Bell and other LECs sponsoring toll tariffs in a competitive market. In the case of

⁹⁷ Case No. 90-431, Petition of AT&T of the South Central States, Inc. for Reduced Regulation of Intrastate Operations.

⁹⁸ Case No. 9889, Adjustment of Rates of AT&T Communications of the South Central States, Inc.

South Central Bell, rates for message toll services must fulfill the requirement of imputed access charges by rate band and time-of-day for calls of average distance and duration. Other toll services must stand a similar test. Moreover, since South Central Bell and the other LECs enjoy access arrangements at least equivalent to the premium access options available to IXCs, imputation should reflect premium access rates.

MCI Building Block Concept

MCI recommended that in the long run a building block concept be used to implement intraLATA toll competition. The building block concept is defined as a procedure requiring standardized costing and pricing based on LEC network functions rather than on specific tariff offerings. MCI advocates implementation of this policy of nondiscriminatory costing to ensure that the benefits of intraLATA competition will be enhanced and that the market will become truly competitive.⁹⁹

The Commission agrees that accurate cost and pricing should be considered in any rate rebalancing proposals filed by the LECs. However, we will not implement any cost allocation approach at this time. At this juncture, we prefer to monitor the intraLATA toll market as it evolves in the short run and make any necessary changes to toll and access pricing as conditions warrant.

Attorney General's Stand-Alone Analysis

Although South Central Bell and others assert that toll rates and/or access charges subsidize local services, the Attorney

⁹⁹ T.E., Volume III, page 131.

General disagrees. He examined each of these services from the perspective of a stand-alone analysis, a procedure that relies on both economic and equity principles. According to this procedure, if revenues from toll or carrier access services were priced above their stand-alone costs, then charges for these services could be reduced if they were supplied on a stand-alone basis. Under such circumstances, a cross subsidy does exist. Alternatively, if the charges for these services were priced below their stand-alone costs, they benefit from the joint supply arrangement with local exchange. Under that condition, in the Attorney General's opinion, cross subsidy does not exist. Using cost data developed by South Central Bell, the Attorney General concludes that toll and carrier access services benefit from the joint provision with local service and no cross subsidy exists.¹⁰⁰

The Attorney General acknowledged that the stand-alone analysis is a relatively new concept which hasn't been used with any frequency and that it is a fairly new way of looking at cost and cross-subsidy issues.¹⁰¹ The Attorney General indicated the analysis was provided to counter South Central Bell's claim that local rates will have to be adjusted if intraLATA competition causes a reduction in toll revenue.¹⁰²

¹⁰⁰ Direct Testimony of Dr. Marvin H. Kahn, filed August 25, 1989, page 5.

¹⁰¹ T.E., Volume VII, page 34.

¹⁰² Id., page 75.

LDDS Route Specific Proposal

LDDS recommended to the Commission that facilities-based competition be phased in on a route-specific basis because it would be beneficial only along high density routes. LDDS argued that this approach would reduce risk to the local ratepayers and increase production efficiency. LDDS also made specific recommendations on how to distinguish competitive and non-competitive routes.

In evaluating LDDS's recommendation, the Commission notes that route restrictions to achieve the efficiency LDDS describes were not imposed in the development of the interstate and interLATA markets. Any duplication of facilities in those markets has not prevented the realization of benefits associated with competition. Also, implementation of LDDS's proposal would likely reduce investment in rural areas. Moreover, market forces will address the problem of inefficient duplication of facilities. Finally, identification of competitive and noncompetitive routes by the Commission would partially shift the burden of determining intraLATA investment to the Commission rather than to the telecommunications industry. This is an artificial barrier which would impede competitive market forces.

Geographical Deaveraging of Toll Rates

In the interLATA market, several non-dominant firms have proposed tariffs with different rates for different geographical

areas. In Case No. 90-154,¹⁰³ the Commission denied tariffs of this type and advised that it would consider the issue of geographical deaveraging of toll rates in this docket. The question was thus posed to all parties, and the parties were unanimous in their response that geographical deaveraging of toll rates was not advisable.

The Commission agrees. It is important that statewide rates be continued, at least for the foreseeable future, to ensure that all areas of Kentucky receive the same benefits of competition. This is true both in the interLATA and intraLATA markets.

Thus, all carriers choosing to provide service in Kentucky in either the interLATA or intraLATA markets must do so by offering uniform prices statewide.

The Geographic Scope of IntraLATA Competition

In its Order dated May 24, 1990, the Commission sought evidence on the appropriate geographic scope of intraLATA competition.¹⁰⁴ Specifically, the parties were asked to address whether competition should be allowed between all exchanges or limited to competition between local calling areas. The parties were also asked to address whether competition should be allowed

¹⁰³ Case No. 90-154, The Tariff Filing of Charter Network Company to Establish Fibermax and Fibercom Supersaver Services.

¹⁰⁴ Administrative Case No. 323, Order dated May 24, 1990, Item 12.

between exchanges where optional calling plans have been implemented.

A local calling area is generally defined as an area within which a subscriber can place calls from one location to other locations without incurring toll charges, and may include more than one exchange. Local calling areas are approved by the Commission and specified in LEC tariffs. In general, the parties contend that competition should be allowed between exchanges or on traffic routes outside the scope of a local calling area and should not be allowed between exchanges or on traffic routes within the scope of a local calling area. Although competition would be maximized by allowing competition between all exchanges irrespective of local calling area designations, valid reasons exist to limit competition within local calling areas. These reasons include, for example, the need to expand local calling areas and eliminate the inhibiting effects of toll charges as extended communities of interest are identified, the need to balance expanded competition with the service obligations of local exchange carriers, and the unlikelihood of successful competition within local calling areas given prevailing rates and rate structures. Therefore, the Commission will presently allow competition between exchanges outside the scope of a local calling area and prohibit competition between exchanges within the scope of a local calling area.

Optional calling plans are LEC-offered measured or flat rate alternatives to the normally applicable toll rate schedule. By definition, optional calling plans are interexchange and

inter-local calling areas. Typically, they provide a discount from prevailing toll rates. Traditionally, they respond to a demand for one-way alternatives to toll rate calling between exchanges. They expand local calling areas by blurring the usual distinction between exchange rate and toll rate calling. Although the availability and popularity of optional calling plans have declined in recent years, there is nothing which prevents LECs from proposing new plans--such as, for example, extended area local measured service.

The few parties that addressed whether competition should be allowed where optional calling plans have been implemented generally support the proposition that competition should be allowed. Consistent with the principle of inter-local calling area competition, the Commission will allow competition between exchanges or on traffic routes where optional calling plans have been or may be implemented, and will rely on market forces to reveal pricing plans proposed by dominant carriers that are anti-competitive in nature.

Equal Access

The Commission sought comment on actions that might be taken to encourage equal access competition in rural and small urban areas of the Commonwealth. The inquiry was prompted by the generally dismal performance of non-dominant IXC's at requesting equal access in these areas. Positive suggestions were few. The parties generally recommended that the Commission take no action and allow equal access to occur at its own pace as competition develops. This is unacceptable. Some 7 years since the inception

of interLATA competition, most LECs have yet to receive their first bona fide request for equal access, even though a number of their central offices are equal access capable. In the Commission's view, equal access should be available to all consumers served by equal access capable central offices.

The Commission has deferred network configuration matters necessary to intraLATA competition to an industry task force. Notwithstanding, the Commission expects LECs to incorporate equal access into their normal network planning activities and deploy equal access generics in equal access capable end offices. Also, the Commission expects IXC's to serve equal access areas on both an originating and terminating basis, and request equal access where it can be made available. To achieve these ends, the Commission will require LECs with end offices that have not been converted to equal access to provide a list of these end offices, whether they are currently equal access capable, and the planned date for equal access conversion. This information should be filed within 30 days from the date of this Order. Thirty days thereafter, the Commission will require non-dominant IXC's to file timetables for seeking equal access in end offices that are not planned for equal access conversion. This information may be of use to the industry task force and will be relevant in the timing of 1+ presubscription.

Regulatory Requirements

Equal regulation of dominant and non-dominant carriers would act as a barrier to entry and expansion of non-dominant carriers,

thus impeding the development of workable and effective competition. Therefore, the Commission will impose on the non-dominant carriers only that amount of regulation required by law and deemed necessary to protect the customer and provide for orderly entrance of companies into the competitive market. By Order of May 25, 1984 in Administrative Case No. 273, the Commission set forth the regulatory requirements for dominant and non-dominant carriers proposing to offer service in the intrastate interLATA market.¹⁰⁵ With few exceptions, the regulatory framework established therein has promoted the development of competition in the interLATA market. The Commission has determined that the same regulatory requirements should be applicable for both inter- and intraLATA services. However, as in the past, the Commission will continue to evaluate and monitor specific services in the telecommunications market and impose conditions as necessary to protect the public interest. Unless otherwise ordered, the regulatory requirements for dominant and non-dominant carrier intrastate intraLATA services should be as herein stated.

Certain modifications to the requirements in Administrative Case No. 273 must be made to comply with current statutory requirements. All statutory requirements will be enforced as to all utilities, with no distinctions made as to dominant and non-dominant carrier.

¹⁰⁵ Administrative Case No. 273, Order dated May 25, 1984, pages 32-37.

All companies certified by this Commission as being dominant carriers for the purposes of providing competitive intraLATA intrastate telecommunications services shall be subject to all the Commission's regulations, 807 KAR Chapter 5. The Commission deems this necessary in order to fully evaluate the pricing and operating policies of dominant carriers in determining whether the tariffs filed by dominant carriers are fair, just, and reasonable.

All companies certified by this Commission as being non-dominant carriers for the purposes of providing competitive intraLATA intrastate telecommunications services shall be subject to an abbreviated form of regulation relative to that applied to dominant carriers. Deviations from compliance with certain Commission regulations will be granted herein, on a continuing basis, to all non-dominant carriers until the Commission regulations can be amended to specifically address non-dominant carriers.

The specific regulations for which non-dominant carriers need not comply unless otherwise ordered by the Commission are as follows:

- 807 KAR 5:001, Section 6, is waived in its entirety. Accordingly, financial exhibits need not be filed by non-dominant carriers.
- 807 KAR 5:001, Section 9(1)(d). The requirement to file a statement showing the need and demand for service is waived for non-dominant carriers.
- 807 KAR 5:001, Section 9(2), concerning new construction or extensions, need not be complied with except as follows: The part of Section 9(2)(c) requiring a full description of the proposed location route or routes of the new construction or extension and Section 9(2)(f) requiring an estimated cost of operation after the proposed facilities are completed.

- 807 KAR 5:001, Section 10, in its entirety. Non-dominant carriers need not file an application to adjust their rates. Rate changes for non-dominant carriers will be accomplished by filing of proposed tariffs.
- 807 KAR 5:001, Section 11, concerning applications for authority to issue securities, notes, bonds, stocks and other evidences of indebtedness need not be complied with by non-dominant carriers except Section 11(1)(b) and (c). Thus, non-dominant carriers shall file a description of the amount and kinds of stock or other evidence of indebtedness, the terms, rate of interest and whether and how the indebtedness will be secured, and a description of the use to be made of the proceeds of the issue.
- 807 KAR 5:006, Section 3, concerning reports, is waived only to the extent that the reports need not be in accordance with the Uniform System of Accounts.
- 807 KAR 5:011, Section 6(2)(c), is waived to the extent that a cost of service study justifying the proposed charges need not be filed by non-dominant carriers.
- 807 KAR 5:011, Section 6(3)(b), the requirement of thirty (30) days' notice to the Commission and the public of new tariffs to the extent described herein. For rate decreases proposed in new tariffs, twenty (20) days' notice to the Commission and the public is permitted. For rate increases and new service offerings, thirty (30) days' notice is required unless a specific deviation is granted by the Commission for the tariff filing.
- 807 KAR 5:011, Section 10, concerning non-recurring charges, except that a copy of the public notice of each rate revision and verification that it has been made pursuant to Section 8 of this regulation shall be filed. The non-dominant carrier shall also mail a copy of its filing to the Attorney General's Consumer Protection Division. Thus, a permanent deviation is granted to non-dominant carriers for the non-recurring charges section except for (1)(b).
- 807 KAR 5:061, Section 15(3), Section 17, and Section 18(5), may be deviated from only upon the non-dominant carrier notifying the Commission in writing as to what the standards of service will be, how these standards will be determined, and upon the non-dominant carrier notifying its customers of the lower quality of service to be offered.
- 807 KAR 5:064, concerning telephone depreciation filing procedures.

Miscellaneous Regulatory Requirements

Certification of Public Convenience and Necessity. In all applications for certification for authority to operate by non-dominant carriers, public convenience and necessity will be assumed to exist absent a showing to the contrary. Any entity filing for a certificate of public convenience and necessity, in addition to the regulations not deviated from herein, will be required to file a showing of financial viability which should include at a minimum a current (within 90 days of filing) income statement (if in operation), a balance sheet and pro forma Kentucky operating statements including the company's potential or forecasted demand and operations for its first 2 years of service. If the company is able to provide a showing of sufficient cash reserves or other financial backing (i.e., line(s) of credit from a bank(s) or other financial institutions, etc.) to sustain the applicant through its initial operating period (2 years), the requirement to provide pro forma operating statements may be waived.

Customer Deposits. Any non-dominant carrier that requires a customer deposit and/or advance payment for service is required to place these funds in an interest-bearing escrow account until the deposit is refunded or, if applicable, service billed in advance has been rendered.

Abandonment. One statute in particular needs mentioning. KRS 278.020(4) requires a utility to seek approval to abandon service. Accordingly, Commission approval is required prior to any portion of a dominant or non-dominant carrier's service

territory or any type of service previously authorized being abandoned.

Report of Minutes of Use. To assist the Commission in evaluating the evolution of the intraLATA toll market, all carriers, dominant and non-dominant, are directed to file minutes of use (Kentucky jurisdictional) by service with this Commission on a quarterly basis. Within 30 days of the date of this Order, an Order will be issued establishing a case in which to file these reports and establishing a reporting format.

ORDERS

The Commission, having considered the evidence of record and being otherwise sufficiently advised, HEREBY ORDERS that:

1. IntraLATA facilities-based toll competition between carriers be and it hereby is authorized.

2. All LECs and IXC's shall comply with the provisions of the Joint Motion and Supplement, attached hereto and incorporated herein, as modified.

3. All LECs and IXC's shall participate in the completion of the scope of work for the Industry Task Force on 1+ presubscription as described herein.

4. A system classifying intraLATA telecommunications carriers as dominant or non-dominant be and it hereby is implemented.

5. The LECs, due to their significant market power in providing intraLATA toll, at this time are dominant carriers for regulatory purposes.

6. AT&T, because of the ease with which it may expand its interstate interLATA operations and marketing program into the LATA's and the competitive advantages it has in the interLATA market, shall be a dominant carrier for regulatory purposes.

7. All telecommunications utilities except for the LECs and AT&T do not have substantial market share and cannot exert pricing power within the LATA and are declared non-dominant carriers for regulatory purposes.

8. Deviations are hereby granted on a continuing basis to all non-dominant carriers for the regulations described herein.

9. All non-dominant intraLATA carriers shall comply with the applicable requirements delineated herein as miscellaneous regulatory requirements.

10. All LECs shall impute the price of access services in their prices of intraLATA toll services.

11. Geographically averaged toll rates shall be maintained.

12. The geographic scope of competition shall extend to the local calling area but not within it.

13. Within 30 days of the date of this Order, LECs shall provide a list of end offices that have not been converted to equal access, a statement as to whether each office is equal access convertible, and the planned date for conversion.

14. Within 60 days of the date of this Order, IXCs, except AT&T and resellers, shall file a timetable for seeking equal access in all end offices.

15. All telecommunications carriers that currently have tariffs on file with the Commission shall make all appropriate tariff changes prior to providing intraLATA services.

16. All intraLATA dominant and non-dominant carriers shall file reports listing minutes of use by service on a quarterly basis. Within 30 days of the date of this Order, an Order will be issued establishing a case in which to file these reports and a reporting format.

Done at Frankfort, Kentucky, this 6th day of May, 1991.

PUBLIC SERVICE COMMISSION


Chairman


Vice Chairman


Commissioner

ATTEST:


Executive Director

ATTACHMENT

ATTACHMENT TO AN ORDER OF THE KENTUCKY PUBLIC
SERVICE COMMISSION IN ADMINISTRATIVE CASE NO. 323 DATED
5/06/91

COMMONWEALTH OF KENTUCKY

BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

JUL 2 1990

In the Matter of:

AN INQUIRY INTO INTRALATA TOLL)
COMPETITION AND APPROPRIATE)
COMPENSATION SCHEME FOR COMPLETION)
OF INTRALATA CALLS BY INTEREXCHANGE)
CARRIERS AND WATS JURISDICTIONALITY)

PUBLIC SERVICE
COMMISSION

ADMINISTRATIVE
CASE NO. 323

SUPPLEMENT TO THE JOINT MOTION
OF A COALITION OF LOCAL EXCHANGE
COMPANIES AND INTEREXCHANGE CARRIERS

The Kentucky Public Service Commission has issued an Interim Order finding that a prima facie case exists that intraLATA competition is in the public interest. The Commission has also set out a procedural schedule pursuant to which it will evaluate implementation issues including consideration of the Joint Motion and any future industry proposals. The Coalition of Local Exchange Companies and Interexchange Carriers¹ (the Coalition) submits this additional information to provide more details on the activities that must take place to accomplish the purpose of the Joint Motion. (Attached hereto for reference)

It is the view of the Coalition that the Joint Motion is consistent with the intent of the Commission's Interim Order and that the Joint Motion represents a fair and reasonable way to implement intraLATA competition in Kentucky. The method

1

All LECs with the exception of South Central Bell, AT&T and US Sprint.

established in the Joint Motion for converting to a competitive intraLATA environment is uncomplicated and it provides for a rapid transition period while at the same time ensuring that a Commission-ordered level of NTS revenue is not diminished. The Coalition continues its unified support for the Joint Motion and provides the following information as a supplement to the initial filing.

A. REQUIRED ACTIVITIES TO IMPLEMENT ACCESS CHANGES AS REQUIRED
IN APPENDIX A & B OF THE JOINT MOTION

1. Access Tariff Changes

- a. Establish LEC specific non-traffic sensitive revenue requirements per access line (Appendix B, page 1 of 2, I.2) together with the supporting information as outlined in Appendix A. Due to the passage of time since the filing of the Joint Motion, these calculations should be based on data for the most recent calendar year for which such data is available at the time of implementation;
- b. Traffic sensitive rates (Appendix A) must be revised to reflect either the current interstate rates for the LEC or the appropriately supported state rates at the time of NTS calculation;

- c. The LECs will develop tariff language specifying the chosen method for recovering the non-traffic sensitive revenue from access users (Appendix B, II);
- d. The Commission's order approving the Joint Motion should specify that access tariff revisions be effective 60 days following the date of the final order and that the ULAS tariff will be superceded on the effective date of the revised tariffs.

2. IntraLATA Pool Settlements

The schedule for changes in traffic sensitive and non-traffic sensitive access rates for intraLATA pool settlements should be implemented on the same schedule as the tariffed access changes.

3. Unblocking of 10XXX

The unblocking of 10XXX does not require any tariff action. However, the LECs will advise their access ordering bureaus that, coincident with the date of the revised access tariffs, interexchange carriers may order access which allows 10XXX intraLATA traffic to be routed to the interexchange carrier.

The above activities describe those functions which must be completed by the effective date specified by the Commission in order to comply with Appendix C, items 1, 2 and 3. These actions will accommodate intraLATA usage for the following IXC type services: (AT&T service names are used for illustrative purposes)

MEGACOM, MEGACOM 800, 800 Readyline, WATS on a 10XXX basis, MultiQuest, Alliance Conference Calling, and DDD on a 10XXX basis including related discount offerings such as Reach-Out and PRO WATS plans.

It is not anticipated that the implementation of these changes will require any modification of the terms and conditions in the existing IXC tariffs. It is not anticipated that any changes will be required in the LEC toll tariffs. Any changes in LEC or IXC tariffs should result only from the need to reflect changes in access costs.

While rate repositioning may be desired by some parties, it would be an independent business decision not necessitated by actions outlined herein.

B. ACTIVITIES REQUIRED SIX MONTHS FOLLOWING THE EFFECTIVE DATE OF THE FINAL ORDER IN PHASE I

1. The local exchange companies will file any required changes in its special access tariff to insure that IXCs are allowed to utilize LEC special access in the provisioning of IXC provided intraLATA private line services.
2. IXCs may file any required tariff changes removing any restrictions relating to providing intraLATA private line services.

3. Whichever party is administering the database for intrastate 800 service will make the necessary changes in its database screening or billing arrangements, whichever is being utilized, to allow statewide IXC 800 service.
4. The IXCs may make tariff changes to offer statewide WATS and/or 800 service arrangements.

C. 1+ DDD PRESUBSCRIPTION

The Coalition believes that the Joint Motion is consistent with the Commission's Order to address 1+ presubscription. The Coalition members are in agreement that the Commission needs to examine a number of areas regarding 1+ intraLATA presubscription. To enable the Commission to make informed decisions regarding this issue, the Coalition proposes that an industry task force be established to examine:

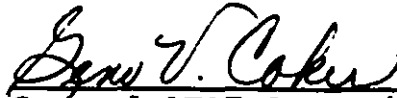
1. The various methods of implementing 1+ presubscription and the technical availability of switching generics to achieve the various methods of implementation together with the cost of each.

2. The potential market changes resulting from 1+ presubscription.

The Commission should schedule hearings to act upon and evaluate the various recommendations and reports developed by the task force.

CERTIFICATE OF SERVICE

It is hereby certified that a copy of the foregoing Supplement to the Joint Motion of a Coalition of Local Exchange Companies and Interexchange Carriers was mailed by first-class United States Mail, sufficient postage prepaid, to all parties of record this 2nd day of July, 1990.

A handwritten signature in cursive script, reading "Gary V. Coker", is written over a horizontal line.

Counsel AT&T Communications of
the South Central States, Inc.

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

RECEIVED

JUL 2 1990

PUBLIC SERVICE
COMMISSION

In the Matter of:

AN INQUIRY INTO INTRALATA TOLL)	
COMPETITION, AN APPROPRIATE)	
COMPENSATION SCHEME FOR COMPLETION)	ADMINISTRATIVE
OF INTRALATA CALLS BY INTEREXCHANGE)	CASE NO. 323
CARRIERS, AND WATS JURISDICTIONALITY)	

SUPPLEMENT TO THE JOINT MOTION OF
LOCAL EXCHANGE COMPANIES AND INTEREXCHANGE CARRIERS

On March 10, 1989, a coalition of the Local Exchange Companies and Interexchange Carriers filed a Joint Motion before the Kentucky Public Service Commission as a proposal addressing intraLATA competition and providing a mechanism to ensure that the Commission ordered level of support derived from both inter and intraLATA toll revenues is not diminished by such competitive expansion.

AT&T Communications of the South Central States, Inc. hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.

AT&T COMMUNICATIONS OF THE
SOUTH CENTRAL STATES, INC.
1200 Peachtree Street, N.E.
Atlanta, Georgia 30309
(404) 873-8700

By:


Gene V. Coker

COMMONWEALTH OF KENTUCKY

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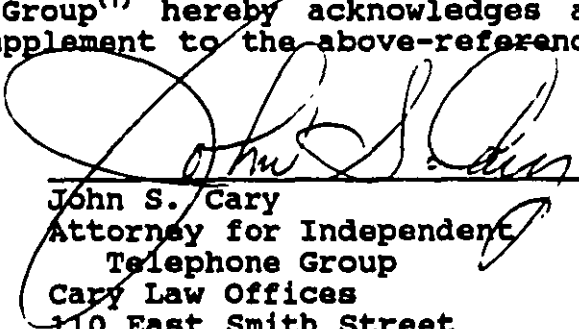
In the Matter of:

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The Independent Telephone Group⁽¹⁾ hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.


John S. Cary
Attorney for Independent
Telephone Group
Cary Law Offices
110 East Smith Street
P. O. Box 777
Burkesville, KY 42717
502-864-3306

⁽¹⁾ Ballard Rural Telephone Coop., Brandenburg Telephone Company, Duo County Telephone Coop., Inc., Foothills Rural Telephone Coop., Harold Telephone Company, Highland Telephone Coop., Logan Telephone Coop., Mt. Rural Telephone Coop., North Central Telephone Coop., Peoples Rural Telephone Coop., South Central Rural Telephone Coop., Thacker & Grigsby Telephone Company, West KY Rural Telephone Coop.

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Cincinnati Bell Telephone Company hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.

CINCINNATI BELL TELEPHONE COMPANY
Post Office Box 2301
Cincinnati, Ohio 45202

By: 

David W. Hills
2500 Central Trust Center
201 East Fifth Street
Cincinnati, Ohio 45202-4182

Attorney for Cincinnati Bell
Telephone Company

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

JUL 2 1990

AN INQUIRY INTO INTRALATA TOLL)
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ADMINISTRATIVE
CASE NO. 323

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ALLTEL Kentucky, Inc. hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.

IVESTER, SKINNER & CAMP, P.A.
111 Center Street, Suite 1200
Little Rock, Arkansas 72201
(501) 376-7788

By: 
H. Edward Skinner

and

LIEBMAN & LIEBMAN
403 West Main Street
Frankfort, Kentucky 40602

By: 
Herbert D. Liebman

Attorneys for ALLTEL Kentucky, Inc.

COMMONWEALTH OF KENTUCKY
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CARRIERS, AND WATS JURISDICTIONALITY)

US SPRINT CONCURRENCE IN SUPPLEMENT TO THE JOINT MOTION OF
LOCAL EXCHANGE COMPANIES AND INTEREXCHANGE CARRIERS

On March 10, 1989, a coalition of the Local Exchange Companies and Interexchange Carriers filed a Joint Motion before the Kentucky Public Service Commission as a proposal addressing intraLATA competition and providing a mechanism to ensure that the Commission ordered level of support derived from both inter- and intraLATA toll revenues is not diminished by such competitive expansion.

US Sprint hereby acknowledges and concurs in the filing of this Supplement to the above referenced Joint Motion.

Respectfully submitted,
US Sprint Communications Company



Michael L. Ball
Donald A. Low
Mary A. Piper
8140 Ward Parkway - 5E
Kansas City, MO 64114
816/276-6879

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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JUL 2 1990

In the Matter of:

PUBLIC SERVICE
COMMISSION

AN INQUIRY INTO INTRALATA TOLL)
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SUPPLEMENT TO THE JOINT MOTION OF
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Contel of Kentucky, Inc. hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.

JACKSON & KELLY
Post Office Box 2150
Lexington, Kentucky 40595-2150
(606) 255-9500

By:



Jeffrey J. Yost
W. Henry Jernigan, Jr.

Counsel for Contel of Kentucky, Inc.

COMMONWEALTH OF KENTUCKY

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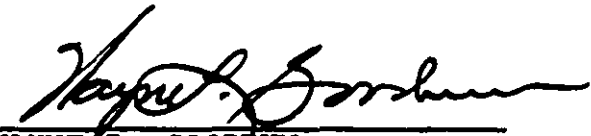
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GTE South Incorporated hereby acknowledges and concurs in the filing of this Supplement to the above-referenced Joint Motion.

GTE SOUTH INCORPORATED

By



WAYNE L. GOODRUM
P. O. Box 110, MC-7
Tampa, Florida 33601
813-228-3085

Its Attorney

COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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JUL 2 1990

PUBLIC SERVICE
COMMISSION

In the matter of:

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OF INTRALATA CALLS BY INTEREXCHANGE)	CASE NO. 323
CARRIERS, AND WATS JURISDICTIONALITY)	

JOINT MOTION OF A COALITION OF
LOCAL EXCHANGE COMPANIES AND INTEREXCHANGE CARRIERS

A coalition of The Local Exchange Companies¹ and Interexchange Carriers² in recognition of the movement of the telecommunications industry toward expanded competition in both the inter and intralATA markets and the consumer benefits of such competition and in recognition of the concerns of regulators and local exchange companies ("LECs") as to the impact of expanded competition on local service rates, move, through counsel, that the Kentucky Public Service Commission ("Commission") accept the proposal of the coalition, which is a part of this motion. The coalition moves the Commission to incorporate the

1. All Local Exchange Companies with the exception of South Central Bell.
2. AT&T, US Sprint.

terms of this motion as part of an initial order in this proceeding, establishing this proposed method of managing non-traffic sensitive revenue as the basis for analyzing and formulating plans for moving the Kentucky telecommunications industry into a more competitive posture.

STATEMENT OF COALITION PROPOSAL

The Joint Motion provides a mechanism that will allow scheduled expansion of competition into the intraLATA interexchange toll markets and, at the same time, ensure that the Commission-ordered level of NTS revenue, which is derived from both inter and intraLATA intrastate toll revenues, is not diminished.

The plan proposed in the Joint Motion is titled "Managing Non-Traffic Sensitive Revenue" ("MNTSR"), is conceptually an expansion of the ULAS concept. With MNTSR, as with ULAS, the non-traffic sensitive (NTS) revenue level is initially authorized and subsequently administered uniquely for each local exchange company. However, with MNTSR the NTS revenue level would include both inter and intraLATA NTS related amounts. This combined NTS revenue level would be recovered uniquely for each LEC from all toll service providers, including the intraLATA pool, resellers, and other parties purchasing switched access, based on each access user's terminating access minutes in that LEC's operating area.

The plan addresses NIS³ related inter and intraLATA access-type revenues, and is designed to accomplish the following objectives:

- 1) allow the scheduled expansion of competition in the intraLATA markets (Appendix C); 2) ensure that expanded competition does not place upward pressure on existing local rates nor on the intraLATA or interLATA toll rates except as minimally required to equalize the per unit contribution of any carrier or the intraLATA pool; 3) provide the Commission with a process to easily and effectively monitor the level of NIS revenue requirement levied on toll services and flowing to each local exchange company by approving the NIS revenue level per access line; 4) provide the Commission with a mechanism to approve the level of toll support provided to any local exchange company without impacting the level of toll support flowing to any other local exchange company; 5) promote the concept of Universal Service.

The plan is designed to work in an environment in which the toll services provided by the LECs are handled through an intraLATA pool or in a non-pooled environment. The plan also accommodates the provision of toll service by a LEC such as Cincinnati Bell, which may administer the provision of toll uniquely for a market area. There are no provisions in this plan to modify any major structures of or participants in the intraLATA pool, nor do the provisions in this plan necessitate any major structural modifications to the intraLATA pool or

3. Administratively the initial NIS authorized level would reflect revenue neutrality from each LEC after mirroring its interstate traffic sensitive rates, including special access rates, for both inter and intraLATA applications.

the manner in which Cincinnati Bell, a non-pooling LEC, may offer the toll service it provides.

Plan development reflects the following postulates:

1) For intraLATA pool participants with the current intrastate access tariffs and intraLATA pool settlement arrangements: the NTS revenue level received from the aggregate of intrastate toll services by each LEC can be determined in the initial year by the formula set forth in Appendix A. In subsequent years the annual NTS revenue level for each LEC would be developed using the number of access lines in service multiplied by the tariffed rate. This would result in the level of NTS support growing as a function of access line growth.

2) The NTS revenue level derived from interLATA toll versus intraLATA toll should be the same per terminating minute and the support level to each LEC should not vary with toll minutes.

3) Each LEC would develop, as a starting point for the plan, its administrative NTS level⁴ per access line per month. The NTS revenue level per access line per month would be filed with the Commission as a part of each LEC's intrastate access tariff.

4) Traffic Sensitive (TS) elements, as used herein, include all categories of intraLATA settlements other than network, billing and collection, carrier common line charges and residual.

4. Any changes in intraLATA private line rates and/or special access rates will be netted out against the calculated NTS level to ensure zero net revenue impact.

5) The recovery of the authorized NIS revenue level would be based on terminating access minutes.⁵ The billing by each IEC to users of access would be done either by developing each access user's percent of total terminating minutes or by developing a rate per access-minute designed to recover the authorized revenue level. These alternative methods are set forth in Appendix B.

6) A IEC may change its traffic sensitive rates in future years by mirroring its own interstate tariffed rates or by supporting its proposed changes by an intrastate-specific cost study.

5. Where calculation of terminating minutes is based on T/O and PIU ratios, the ratios used must be the same as the ratios used for billing upon implementing this plan.

REVENUE STARTING POINT FOR INTRALATA POOL COMPANIES AND CINCINNATI BELLINTRALATA POOL COMPANIES

1.	INTERLATA	LEC'S TOTAL		SWITCHED QxP(new) ¹		
	STARTING POINT ³	=	1988 INTERLATA TOLL REVENUE	LESS	SPECIAL ACCESS QxP(new) ²	= INTERLATA NTS REVENUE LEVEL
					BILLING & COLLECTION QxP(existing)	
2.	INTRALATA	LEC'S TOTAL 1988		SWITCHED QxP (new) ¹		
	STARTING POINT	=	INTRALATA TOLL SETTLEMENTS INCLUDING PRIVATE LINE SETTLEMENTS	LESS	PRIVATE LINE QxP (new) ²	= INTRALATA NTS REVENUE LEVEL
					NETWORK QxP(existing)	
					BILLING & COLLECTION QxP(existing)	

STARTING POINT TOTAL NTS REVENUE LEVEL = 1 + 2

CINCINNATI BELL

3.	INTERLATA					
	STARTING POINT	=	INTERLATA CCLC * INTERLATA MOUs + ULAS			= INTERLATA NTS REVENUE LEVEL
4.	INTRALATA					
	STARTING POINT	=	EFFECTIVE INTERLATA RATE * INTRALATA MOUs			= INTRALATA NTS REVENUE LEVEL

STARTING POINT TOTAL NTS REVENUE LEVEL = 3 + 4

1. New switched quantities must be calculated using T/O and PIU ratios in effect at the time of plan implementation.

2. Any changes in intraLATA private line rates and/or special access rates will be netted out against the calculated NTS level to ensure zero net revenue impact.

3. GTE believes that IXC leases need to be addressed to determine proper disposition in this plan.

XYZ TELEPHONE COMPANY - MANAGING NON-TRAFFIC SENSITIVE REVENUE

I. NTS REVENUE LEVEL DETERMINATION

1. STARTING POINT TOTAL NTS REVENUE LEVEL (FROM APPENDIX A)
2. PER ACCESS LINE MONTHLY NTS FILED RATE=
TOTAL NTS LEVEL (LINE 1)/MID-YEAR 1988 ACCESS LINE¹ COUNT/12

II. LEC BILLING OPTIONS FOR RECOVERING NTS REVENUE FROM ACCESS USERS
(TWO METHODS MAY BE USED)

1. METHOD A (PERCENT DISTRIBUTION METHOD)

MONTHLY CALCULATION OF CARRIER DISTRIBUTION:

A	B	C
<u>CARRIER</u>	<u>TERMINATING ACCESS MOU²</u>	<u>DISTRIBUTION</u>
1. INTRALATA POOL	1B	1B/TOTAL B
2. FACILITY BASED X	2B	2B/TOTAL B
3. FACILITY BASED Y	3B	3B/TOTAL B
4. NON-FACILITY BASED A	4B	4B/TOTAL B
5. NON-FACILITY BASED B	5B	5B/TOTAL B
6. OTHER ACCESS USERS	6B	6B/TOTAL B
	<u>TOTAL</u>	<u>1.0</u>

¹THE DEFINITION OF ACCESS LINES WILL BE THE SAME AS THAT USED FOR REPORTING ACCESS LINES TO NECA ON LINE 2 OF EITHER FORM EC1000 OR EC1050, OR THE EQUIVALENT NUMBER FOR NON-NECA REPORTING COMPANIES. CENTREX LINES WILL HAVE AN EQUIVALENT ADJUSTMENT TO PROVIDE PARITY WITH PBX TRUNKS.

²WHERE CALCULATION OF TERMINATING MINUTES IS BASED ON T/O AND PIU RATIOS, THE RATIOS TO BE USED MUST BE THE SAME AS THE RATIOS USED FOR BILLING IN EFFECT UPON THE DATE THIS PLAN IS IMPLEMENTED.

II. LEC BILLING OPTIONS FOR RECOVERING NTS REVENUE FROM ACCESS USERS

2. METHOD B (PER MINUTE RATE METHOD)

A. FORECAST ALTERNATIVE

PER MINUTE RATE BILLED TO ACCESS USERS=
(AVERAGE NUMBER IN-SERVICE ACCESS LINES x FILED RATE x 12)/FORECASTED
TERMINATING ACCESS MINUTES

RATE WILL BE TRUED-UP SEMI-ANNUALLY IF NEEDED.
RATE WILL BE RECALCULATED ANNUALLY.

B. HISTORICAL ALTERNATIVE

PER MINUTE RATE BILLED TO ACCESS USERS=
(PREVIOUS YEAR AVERAGE IN-SERVICE ACCESS LINES x FILED RATE x
12)/PREVIOUS YEAR TERMINATING ACCESS MINUTES

RATE WILL BE TRUED-UP ANNUALLY
RATE WILL BE RECALCULATED ANNUALLY

NOTES: WHEN ONE LEC PROVIDES INTRASTATE FGA/B TERMINATING TRAFFIC AND BILLING FOR THAT TRAFFIC FOR ANOTHER LEC, THE SECONDARY LEC WILL BILL THE PRIMARY LEC FOR TERMINATING MINUTES AT ITS NTS SUPPORT RATE, OR THE RECORDING (PRIMARY) LEC WILL PROVIDE THE BILLING INFORMATION TO THE SERVING (SECONDARY) LEC FOR BILLING TO THE ACCESS USER.

IF ACCESS LINES DECREASE, THE TOTAL SUPPORT LEVEL WILL NOT DECREASE. HOWEVER, IN THE EVENT OF SUCH NEGATIVE ACCESS LINE GROWTH, THE TOTAL SUPPORT LEVEL WILL NOT BE INCREASED UNTIL FUTURE GROWTH SURPASSES THE EARLIER LEVEL FROM WHICH DECREASES WERE CALCULATED.

SCHEDULE OF INTRALATA COMPETITION

Customer options will be increased via expanded IntraLATA competition in accordance with the following schedule. Charges to users of access services (toll service providers and other users of access) will be those set forth in the respective LEC access tariffs.

Service descriptions of the IXCs vary significantly, consequently it is necessary to identify allowed areas of intraLATA competition according to access connection arrangements. The schedule identifies access arrangements where competition is allowed, many of the access connections currently allow intraLATA usage. This proposed expansion of competition does not change or alter in any manner the allowable servicing arrangements for resellers nor would it restrict the service capabilities of resellers beyond the restrictions applied to interexchange carriers as a result of the adoption of this motion.

Effective Date of Phase I order (Proposed 9-1-89)

1. The initial expansion of intraLATA competition consists of approval on a permanent basis of IXC services presently authorized by interim Commission approval and allowing customers to access all IXCs via IXCs carrier access code (10XXX). The 10XXX access is currently allowed for some carriers but not all. This results in the following allowable dialing arrangements.
 - FG A NXX-XXXX,
(No change - currently allowed)
 - FG B 950-XXXX
(No change - currently allowed)
 - FG D Carrier Access Code 10XXX 1+ or 10XXX 0- or 10XXX 0+
(Currently allowed for resellers, but not for IXCs.)
 - FG D 1-700/800/900 access allowed for services other than 800 Service offered as an add-on to LEC provided 800 Service
(No change for existing add-on 800 Service)
 - FG C 1-700/800/900 access allowed for services other than 800 Service which is offered as an add-on to LEC provided 800 Service. All other FG C services are presently reserved for the LECs.
(No change for existing add-on 800 Service)
2. Customers are not at this time allowed to presubscribe their intraLATA 1+ DDD calling to other than the Local Exchange Company.

3. Customers are allowed to utilize interexchange carriers or resellers for the completion of outgoing or incoming billed intraLATA traffic (which is offered as a part of a total service including inter and intraLATA usage as one service) by accessing their carrier of choice, and these carriers are allowed to offer such services using access arrangements which directly connect the customer to the interexchange carrier or reseller location.
(No change for existing services, this arrangement allowed for IXC services with interim Commission approval)

Six months following the effective date of Phase I order (proposed date 3-1-90)

1. Customers will be allowed to purchase intraLATA private line services¹ from interexchange carriers and these carriers will be allowed to offer such services. For IntraLATA private line services, the IXCs must purchase the access to the end users from the LECs.
2. Customers will be allowed the option of purchasing, and interexchange carriers and resellers will be allowed to offer state-wide WATS and 800 Services in addition to the existing add-on arrangements defined previously.

Two years following the effective date of the Phase I order (Proposed date 9-1-91)

1. The Commission will review further expansion of competition into the intraLATA market including presubscribed 1+ DDD calling.

1. IntraLATA private line services are defined as private line services which originate and terminate within the LATA and are not used as a part of an interLATA network and are used to make only intraLATA customer connections.